

Internal Revenue Service

Number: **202007014**

Release Date: 2/14/2020

Index Numbers: 1362.00-00, 1362.01-00,
1362.01-01, 1362.04-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:03

PLR-111922-19

Date:

November 12, 2019

Legend

Company =

Trust =

Trust 1 =

Trust 2 =

A =

B =

State =

Date 1 =

Date 2 =

Date 3 =

Dear _____ :

This letter responds to a letter dated May 14, 2019, and subsequent correspondence, submitted on behalf of Company by its authorized representative requesting a ruling under §1362(f) of the Internal Revenue Code (Code).

Facts

According to the information submitted, Company was incorporated under the laws of State on Date 1 and made an election to be treated as an S corporation effective Date 2. Under Trust, separate trusts, Trust 1 and Trust 2 for the benefit of A and B respectively, owned shares of Company stock on Date 2. It is represented that as of Date 2, Trust 1 and Trust 2 satisfied the qualified subchapter S trust (QSST) requirements under §1361(d)(3). In Date 3, Company learned that A and B, the income beneficiaries of Trust 1 and Trust 2, respectively, each failed to make an election to treat their respective trusts as QSSTs effective Date 2. In addition, Company learned that the trustee of Trust and not A and B consented to Company's S corporation election on its Form 2553, Election by a Small Business Corporation. Therefore, Company's S corporation election was ineffective.

Company represents that Company and its shareholders have filed tax returns consistent with Company having a valid S corporation election in effect as of Date 2. Company and its shareholders have agreed to make any adjustment that the Commissioner may require, consistent with the treatment of Company as an S corporation.

Law and Analysis

Section 1361(a)(1) provides that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under §1362(a) is in effect for such year.

Section 1361(b)(1)(B) provides, in part, that, for purposes of subchapter S, the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not have as a shareholder a person (other than an estate, a trust described in §1361(c)(2), or an organization described in §1361(c)(6)) who is not an individual.

Section 1361(c)(2)(A)(i) provides that, for purposes of §1361(b)(1)(B), a trust all of which is treated (under subpart E of part I of subchapter J of chapter 1 of the Code) as owned by an individual who is a citizen or resident of the United States may be a shareholder.

Section 1361(d)(1) provides that in the case of a QSST with respect to which a beneficiary makes an election under §1361(d)(2), the trust is treated as a trust

described in §1361(c)(2)(A)(i), and for purposes of §678(a), the beneficiary of such trust shall be treated as the owner of that portion of the trust which consists of stock in an S corporation with respect to which the election under §1361(d)(2) is made. Section 1361(d)(2)(A) provides that a beneficiary of a QSST may elect to have §1361(d)(1) apply.

Section 1361(d)(3) defines a QSST as a trust, (A) the terms of which require that (i) during the life of the current income beneficiary, there shall be only one income beneficiary of the trust, (ii) any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary, (iii) the income interest of the current income beneficiary in the trust shall terminate on the earlier of such beneficiary's death or the termination of the trust, and (iv) upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to such beneficiary, and (B) all of the income (within the meaning of §643(b)) of which is distributed (or required to be distributed) currently to one individual who is a citizen or resident of the United States.

Section 1362(a)(1) provides that, except as provided in §1362(g), a small business corporation may elect, in accordance with the provisions of §1362, to be an S corporation.

Section 1362(a)(2) provides that an S corporation election shall be valid only if all persons who are shareholders in such corporation on the day on which such election is made consent to such election.

Section 1.1362-6(b)(2)(iv) of the Income Tax Regulations provides that in the case of a trust described in §1361(c)(2)(A) (including a trust treated under §1361(d)(1)(A) as a trust described in §1361(c)(2)(A)(i) and excepting an electing small business trust described in §1361(c)(2)(A)(v)), only the person treated as the shareholder for purposes of §1361(b)(1) must consent to the election.

Section 1.1361-1(j)(7)(i) provides that the income beneficiary who makes the QSST election and is treated (for purposes of §678(a)) as the owner of that portion of the trust that consists of S corporation stock is treated as the shareholder for purposes of §§1361(b)(1), 1366, 1367, and 1368.

Section 1362(f) provides that if (1) an election under §1362(a) or §1361(b)(3)(B)(ii) by any corporation (i) was not effective for the taxable year for which made (determined without regard to §1362(b)(2)) by reason of a failure to meet the requirements of §1361(b) or to obtain shareholder consents, or (ii) was terminated under §1362(d)(2) or (3) or §1361(b)(3)(C); (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent; (3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken so that the corporation for which the election was made or the termination occurred is a small business corporation or a qualified subchapter S

subsidiary (QSub), as the case may be, or to acquire the required shareholder consents; and (4) the corporation for which the election was made or the termination occurred, and each person who was a shareholder of the corporation at any time during the period specified pursuant to §1362(f), agree to make the adjustments (consistent with the treatment of the corporation as an S corporation or a QSub, as the case may be) as may be required by the Secretary with respect to this period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, the corporation shall be treated as an S corporation or a QSub, as the case may be, during the period specified by the Secretary.

Conclusion

Based solely on the facts submitted and the representations made, we conclude that Company's S corporation election was ineffective on Date 2 because A and B failed (1) to file a QSST election for Trust 1 and Trust 2, respectively, and (2) to consent to Company's S corporation election. We further conclude that the ineffectiveness of Company's S corporation election constituted an inadvertent invalid election within the meaning of §1362(f). Consequently, under §1362(f), we rule that Company will be treated as an S corporation from Date 2 and thereafter, provided that Company's S corporation election was otherwise valid and not otherwise terminated under §1362(d).

This ruling is contingent on A and B filing a QSST election for Trust 1 and Trust 2, respectively, effective Date 2, with the appropriate service center within 120 days from the date of this letter. A copy of this letter should be attached to each QSST election. In addition, as a condition to this ruling, A and B must sign a written statement as described in §1.1362-6(b)(1) consenting to Company's S corporation election effective Date 2. The written statement(s) must be filed with the appropriate service center within 120 days from the date of this letter, indicating that the statement(s) is to be associated with Company's originally filed Form 2553.

Except as specifically ruled above, we express or imply no opinion as to the federal income tax consequences of the facts described above under any other provision of the Code, including whether Company was otherwise a valid S corporation or whether Trust 1 and Trust 2 are valid QSSTs.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the ruling request, it is subject to verification on examination.

Pursuant to a power of attorney on file with this office, we are sending a copy of this letter to your authorized representatives.

Sincerely,

Mary Beth Carchia
Senior Technician Reviewer, Branch 3
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2):
Copy of this letter
Copy for §6110 purposes

cc: